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THE SUMMATION APPROACH TO THE VALUATION OF A SERVICE STATION

IN June we published an Appraisal Bulletin which discussed some of the general problems involved in appraising service stations. In November the Appraisal Bulletin included construction costs of service stations and their improvements. That bulletin gave material for the first step in the service station appraisal process by the summation approach - that of estimating the replacement cost of the improvements. This bulletin will describe the appraisal process by the summation approach to the valuation of a service station.

The land valuation generally is secured by the comparative method in combination with the land residual method of the income approach. Often, land used by a service station will produce a higher value than it would for any other use. This is particularly true for sites in good residential districts or for sites along highways in rural areas. Often, a good site is reduced in value by competitive stations locating in the same area.

In some cities, special permits are issued under restrictive ordinances which limit the location of service stations. Under such conditions, in addition to land value, the site may take on a permit value. The value of the permit is determined by the location of the site, its environs, and the conditions which limit competition. In a good residential area, for instance, spot zoning which would permit a service station would give the site a permit premium. This premium might be worth thousands of dollars if the station were assured limited competition, but would be worth relatively little if there were a number of adequate vacant sites similarly zoned which could be used for service stations. For an existing station with known operating experience, the income approach is the best method of measuring the value of the permit. The value of the station estimated by the income approach less the depreciated value of the improvements and the value of the land secured by the comparative approach results in the permit value, but it may also include the value of good will or the value of a going concern. In some cases it is almost impossible to filter out the net return imputable to the real estate. In the case of low-volume stations, there is no premium for its permit nor for its enterprise.

In appraising the site, it is important to consider the elements affecting value. The site should be adequate in size, shape, and topography. The minimum

site size of a few years ago, 100' x 100' , is now considered too small; 125' to 150' is presently considered minimum in urban areas, with 200' frontage along highways or major traffic arteries. Minimum depths may vary from 75' to 125' , depending on location and the station's requirements. In order to be adequate, the site should be level, at street grade, and roughly rectangular in shape to afford ease of entrance and exit. The American motorist is as lazy as he is impatient, and will patronize the most convenient station that will give the best service, quickest and at the price he is willing to pay. For years it was conceded that the close right-hand corner of the street on the way toward town was the choicest site. In the past decade, however, electric traffic signals have been placed at most busy intersections, backing up traffic until these once excellent sites no longer hold the premium they did in the past. These traffic signals have made some stations in urban areas relatively inaccessible.

The application of unit construction costs to the specifications of the improvements included on the subject property gives reconstruction costs new. These costs are extremely high today and will probably average about $30,000 for a new 2-bay station, in the average residential location. Of course, this figure will vary with the type of station. Stations in rural districts, for instance, along highways that primarily serve tourists, seldom have expensive grease bays and wash racks, as their income is primarily derived from gasoline sales. These stations generally have more pumps than the neighborhood station.

Generally, it is conceded that maximum value is the sum of the value of the land (which includes the permit premium) and the replacement cost new of the improvements. A lease favorable to the owner would be an additional premium that would increase this maximum value. In appraising service stations it must be remembered that the value is predicated on average management and not on excellent or poor management.

Once the replacement cost is estimated, it is necessary to estimate the amount of accrued depreciation. Depreciation may be divided into three types: physical deterioration, functional obsolescence, and economic depreciation.

Physical deterioration is evidenced by wear and tear, rot, encrustations, cracks or structural deterioration. These defects may be normal or excessive, or minimized by excellent maintenance. Structurally, service stations, properly maintained, should have approximately the same life as other buildings. A 1 to 2% per year rate for deterioration should suffice. Structural faults or poor maintenance could increase this rate. Major oil companies and the Internal Revenue Service, however, generally accept the life of a station to be 20 to 25 years. The oil companies prefer writing off their investments at this rapid rate because of tax benefits, and the Government's having accepted this practice caused the practice to be generally accepted. We would like to emphasize our belief that service stations have a greater structural life than this. The actual accrued depreciation is primarily a matter of functional obsolescence rather than physical deterioration. Physical deterioration should be based on the appraiser's observation

of the structure and its physical condition. We believe that the average physical life of a new structure is 50 years, despite the fact that it probably will become obsolete at an earlier date and be wrecked.

Functional obsolescence, to a great extent in recent years, has been caused by the increase in construction costs of service station improvements and the high wages of attendants. As a result, to economize, gasoline distribution firms have built stations with greater facilities on larger sites, with more pumps to serve more cars at a lower unit cost. In addition, the multipump station with automatic nozzle feed and cut-offs can serve more gasoline with fewer attendants. This reduces the labor costs per vehicle served. Some of the multipump stations have far more pumps than they have personnel to man them. Nevertheless, they do attract the impatient motorist who can readiiy drive up to a pump without waiting in line. As a result of this recent trend, stations with limited pumping facilities, particularly when located on small sites, are now considered obsolete, despite the condition of the improvements. Such stations might be considered on the same basis as an overimprovement for the size of the site, another item of functional obsolescence.

As pointed out earlier, accessibility is one of the prime requisites of a good site. Traffic congestion and high-speed traffic tend to restrict ease of entrance and exit, and are considered depreciating - an item of functional obsolescence. The amount of this obsolescence may vary to 100% in the event that the street or highway serving the station was made a freeway and access was totally restricted. The actual extent of the obsolescence must be estimated by the appraiser. He may attempt to measure the amount of loss by comparing business before and after, or comparing sales volumes of other stations. It should be kept in mind that any percentage drop in the total volume of a filling station will affect the property by a greater percentage, as many items in the operation of a station are fixed expenses regardless of volume. As the volume decreases, the unit cost for overhead increases. Of course, poor planning and styling of the structure and obsolete equipment are the generally accepted items of functional obsolescence.

Economic depreciation generally is caused by changes outside of the property itself, such as incongruity of neighboring properties as to type of use, the infiltration of an inharmonious population, excessive competition, restrictive legislation, etc.

An example of economic depreciation sometimes used in discussing filling stations is the case where a pioneering station develops a large gallonage in a good location. This gallonage attracts a number of other stations which locate in the vicinity, and because of the excess capacity of the group of stations, all suffer. It is probably only approximately correct to attribute all of the loss of volume to economic depreciation in this case. A part of the former volume was due to a monopoly value which the station originally had. This value disappeared when competition arrived. In fact, the value of the site previously

described in this bulletin as a permit value is in many cases a monopoly value, made possible by the limited number of sites which zoning or permit limitations made available.

Another example of economic depreciation would occur if State or Federal highways were rerouted, reducing traffic flow past the site. Sometimes converting a 2-way street into a 1-way street destroys a large part of the value of a site for filling station use.

We would like to point out again that not only are the improvements subject to depreciation, but the value of the land may also change because of changes in zoning restrictions, changes in accessibility, or in neighborhoods. The appraiser must always be on the alert not only to detect the existing conditions that affect value, but he should also be informed as to probable future developments. He should remember that present value is based on the present worth of all future benefits which can be derived from ownership. The past experience of a station is valuable, but only as a guide to its probable future.

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